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No. 89-1360

In The

Supreme Court of the United States

October Term, 1990

ALLAN DEVORE,

Petitioner,

v.

STEPHEN R. KERR AND
WILLIAM O. JOHNSTONE,

Respondents.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Respondents, Stephen R. Kerr and William O. Johnstone, submit this Brief in Opposition to Petitioner, Allan Devore's Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit ("Petition").

STATEMENT OF THE CASE

On February 12, 1988, a lawsuit was filed by the Petitioner, Allan Devore, for his clients, Hill Resources, Inc., Irving A. Hill, and Ronald M. Hill (the "Hills"), against the Respondents, Stephen R. Kerr and William O. Johnstone, and other defendants, based on common law fraud and 18 U.S.C. § 1961-62 ("RICO"), with the alleged predicate act of mail fraud under 18 U.S.C. § 1341. On September 13, 1988, the United States District Court for the Western District of Oklahoma granted Respondents' motion to dismiss treating it as a summary judgment. On September 26, 1988, the district court granted a motion to dismiss filed by two of the other defendants, United Oklahoma Bankshares, Inc. ("UOB") and Morrison G. Tucker, and authorized the Petitioner to file an amended complaint as to such other defendants. On September 27, 1988, the Petitioner filed, for his clients, a motion to reconsider the court's ruling dated September 13, 1988. On October 6, 1988, the Petitioner also filed, for his clients, an amended complaint naming Respondents and other defendants as parties. On October 19, 1988, the district court denied the September 27, 1988, motion to reconsider.

On December 1, 1988, the district court granted Respondents' motion for sanctions and awarded attorney's fees and costs against Petitioner and his clients. The district court awarded sanctions based on its finding that Petitioner had violated Rule 11 of the Federal Rules of Civil Procedure ("Rule 11," a copy of which is annexed hereto as Appendix A) by filing a complaint and an amended complaint without making reasonable inquiry to determine if such pleadings were well grounded in fact

and were warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law. A concise, detailed statement of facts may be found in the April 20, 1989 Brief of Appellees - Appeal from United States District Court for the Western District of Oklahoma ("Brief of Appellees"), which is incorporated by reference herein. To avoid duplication of effort and as an aid to the Court, the statement of facts contained in the Brief of Appellees ("Statement of Facts") is annexed hereto as Appendix B.

On appeal, the Tenth Circuit Court of Appeals affirmed the district court's judgment, holding that the district court had not abused its discretion in awarding sanctions against the Petitioner and his clients.

SUMMARY OF ARGUMENT

The present case is not appropriate for review by the Supreme Court of the United States for several reasons. First, the Tenth Circuit Court of Appeals has rendered an opinion based on "abuse of discretion" as its standard of review for Rule 11 issues. "Abuse of discretion" has been adopted by at least half of the circuit courts as the standard of review for all Rule 11 issues. All remaining circuit courts have incorporated "abuse of discretion" as part of an appropriate standard of review with regard to Rule 11 issues. Deference to the district court, as is inherent in the "abuse of discretion" standard, is appropriate in this situation, since it avoids duplication of effort, recognizes that fact-bound decisions cannot be made uniform by

appellate court review, and avoids distortion of the issues of law subject to review.

Second, the Petitioner's argument that the wrong standard of review was used demonstrates, at most, harmless error. Here, Petitioner was unable, at the sanction hearing, to offer any evidence of investigative or discovery material reviewed prior to filing the complaint, notwithstanding the existence of a prior, nearly identical case. In fact, Petitioner neither testified in his own behalf nor called any expert witness. The only two non-party witnesses called by Petitioner at the sanction hearing concede that they first met Petitioner and related their testimony on the very morning of the sanction hearing. In addition, Petitioner alleged in the complaint a claim that was precluded as a matter of law. Finally, Petitioner filed an amended complaint naming Respondents after Respondents had been granted judgment on the merits. In the face of Petitioner's complete failure to evidence the existence of any reasonable inquiry, it cannot be said his substantive rights were abused. Thus, no substantial rights of the Petitioner were affected by the use of "abuse of discretion" as the standard of review.

Third, the Petitioner's argument that the substantive law of amended complaints controls procedural law is of no consequence. When Petitioner filed the amended complaint naming Respondents, the Respondents had already obtained a judgment on the merits in their favor! It is inconceivable that the Court shall ever encounter another Rule 11 case where the record so clearly demonstrates an absence of reasonable inquiry both as to factual and legal issues. No conceivable standard of review would alter the district court's conclusion that such a compelling absence

of any showing of reasonable inquiry justified the imposition of sanctions under Rule 11. The Petitioner has presented an interesting question with regard to standards of review. Respondents respectfully submit, however, that this case is singularly inappropriate for the issuance of a writ of certiorari because of the inescapable conclusion that Rule 11 sanctions were justified under any standard of review.

ARGUMENT

I

NO SUBSTANTIAL RIGHTS OF THE PETITIONER WERE AFFECTED BY THE COURT OF APPEALS' CHOICE OF "ABUSE OF DISCRETION" AS THE STANDARD OF REVIEW FOR RULE 11 ISSUES.

A. Abuse of Discretion was a Correct Standard of Review.

The Tenth Circuit Court of Appeals has adopted an "abuse of discretion" standard of review on all Rule 11 issues. *Adamson v. Bowen*, 855 F.2d 668, 673 (10th Cir. 1988); *Burkhart v. Kinsley Bank*, 852 F.2d 512, 515 (10th Cir. 1988); *Cotner v. Hopkins*, 795 F.2d 900, 903 (10th Cir. 1986); *Chevron, USA, Inc. v. Hand*, 763 F.2d 1184, 1187 (10th Cir. 1985). At least half of the circuit courts apply the "abuse of discretion" standard to all Rule 11 issues. *Mars Steel Corp. v. Continental Bank, N.A.*, 880 F.2d 928, 930 (7th Cir. 1988); *Adamson v. Bowen*, 855 F.2d 668, 673 (10th Cir. 1988); *Thomas v. Capital Security Services, Inc.*, 836 F.2d 866, 872 (5th Cir. 1988); *Century Products, Inc. v. Sutter*, 837 F.2d 247, 253 (6th Cir. 1988); *EBI, Inc. v. Gator Indus., Inc.*,

807 F.2d 1, 6 (1st Cir. 1986); *Stevens v. Lawyers Mut. Liab. Ins. Co.*, 789 F.2d 1056, 1060 (4th Cir. 1986); *cf. Snow Machines, Inc. v. Hedco, Inc.*, 838 F.2d 718, 724-25 (3rd Cir. 1988). Thus, the Tenth Circuit's choice of "abuse of discretion" is well-supported by the weight of authority.

The remaining circuit courts are split on the standard of review. One view embraces a "three-pronged" standard of review: (1) factual determinations of the district court are reviewed under a clearly erroneous standard; (2) the legal conclusion of the district court that the facts constitute a violation of Rule 11 is reviewed *de novo*; and (3) the appropriateness (i.e. the type or amount) of the sanction is reviewed for an "abuse of discretion." *McMahon v. Shearson/American Express, Inc.*, Westlaw 14776, ___ F.2d ___ (2nd Cir. 1990); *Equal Employment Opportunity Comm'n. v. Milavetz and Associates*, 863 F.2d 613, 614 (8th Cir. 1988); *Zaldivar v. City of Los Angeles*, 780 F.2d 823, 828 (9th Cir. 1986). The other view endorses a standard of review which differs depending on the question before the court. District court decisions on the legal sufficiency of a pleading or motion are considered questions of law and are reviewed *de novo*. District court decisions as to whether factual or bad faith reasons existed to impose Rule 11 sanctions and on the appropriateness (i.e. the type or amount) of the particular sanction are reviewed only for an "abuse of discretion." *Donaldson v. Clark*, 819 F.2d 1551, 1556 (11th Cir. 1987); *Westmoreland v. CBS, Inc.*, 770 F.2d 1168, 1174-75 (D.C. Cir. 1985). The use of "abuse of discretion" as the standard of review at some point in each of these two views indicates the acceptability of "abuse of discretion" as a standard of

review for Rule 11 issues, even among those circuit courts which do not use it across the board for all Rule 11 issues.

Respondents submit the "abuse of discretion" standard of review was appropriate in Petitioner's case, and deference to the district court was appropriate, as can be demonstrated by analogy to a case recently decided by this Court, *Pierce v. Underwood*, 487 U.S. ___, 108 S.Ct. 2541, 2546-49, 101 L.Ed.2d 490 (1988). In *Underwood*, the Court held that courts of appeals should use an "abuse of discretion" standard of review when assessing a district court's conclusion under the Equal Access to Justice Act, 28 U.S.C § 2412(d), as to whether the government's litigating position is "substantially justified." "Abuse of discretion" was chosen as the standard of review because, in part, it allows for deference to the district court. With regard to legal questions, the *Underwood* court stated:

> [S]ome cases . . . will involve a judgment ultimately based upon evaluation of the purely legal issue governing the litigation. It cannot be assumed, however, that *de novo* review of this will not require the appellate court to invest substantial additional time, since it will in any case have to grapple with the same legal issue on the merits. . . .[To the contrary, on a merits appeal] the latter legal question will not be precisely the same as the merits: not what the law now is, but what the Government was substantially justified in believing it to have been. In all the separate-from-the-merits EAJA appeals, the investment of appellate energy will either fail to produce the normal law-clarifying benefits that come from an appellate decision on a question of law, or else will strangely distort the appellate process. . . .
>
> . . . .

> [An additional reason for the deferential review of a district court decision is] that the question whether the Government's litigating position has been "substantially justified" is precisely such a multifarious and novel question, little susceptible, for the time being at least of useful generalization, and likely to profit from the experience that an abuse-of-discretion rule will permit to develop.

108 S.Ct. at 2547-48. These considerations are of equal importance in Rule 11 cases and weigh heavily in favor of the use of "abuse of discretion" as the standard of review for all Rule 11 issues. In addition, deference on the part of this Court to the district court decision in the present case, as would be evidenced by the denial of the Petition, would be consistent with the considerations warranting deferential review expressed by the Court in *Underwood*.

The Seventh Circuit Court of Appeals endorsed the practice of giving deference to district court decisions on Rule 11 issues, when it adopted "abuse of discretion" as the standard of review for all Rule 11 issues in *Mars Steel Corp.* The court stated:

> Many judges and lawyers are concerned about the lack of uniformity in the application of Rule 11. . . . Fact bound resolutions cannot be made uniform through appellate review, de novo, or otherwise. . . . [C]ase-specific decisions should be made in the trial courts and reviewed on a deferential standard. The judgment of three appellate judges is not necessarily better than the judgment of one district judge, but it is assuredly more costly to obtain and interpret.

880 F.2d at 936 (citations omitted). *Mars Steel* endorses "abuse of discretion" as the standard of review for Rule 11 issues because it is a deferential standard. Deference to

the district court decision in the present case would be consistent with the rationale given in *Mars Steel* for choosing a deferential standard of review.

Although "abuse of discretion" is not the only possible standard of review for Rule 11 issues, "abuse of discretion" is *a* correct standard of review. At least half of the circuit courts apply the "abuse of discretion" standard of review to all Rule 11 issues. Even among those courts which do not use the "abuse of discretion" standard of review for all Rule 11 issues, "abuse of discretion" is still the appropriate standard of review at some point in the review of Rule 11 issues. When deference is not given to the trial court, as in the case of a *de novo* review, a costly duplication of effort is required; yet the appellate court will never be able to recreate to perfection the facts and the questions of law as they once existed before the trial court. Deference to the trial court avoids this distortion. Similarly, deference on the part of this Court to the district court in the present case by denying the Petition would be consistent with the considerations discussed by the Court in *Underwood* and by the Seventh Circuit in *Mars Steel*.

B. Regardless of the Particular Standard of Review Chosen, the Sanctions Against Petitioner Would Be Upheld.

The Petitioner's argument that the wrong standard of review was applied to the Rule 11 issues presented on appeal will, at most, demonstrate harmless error. A harmless error includes those errors which were merely academic, which did not prejudice the substantial rights of

the appellants, and which did not affect the outcome of the case. *State v. Button*, 178 P.2d 341, 345 (Wash. 1947). An error is harmless when it does not injure the substantive rights of the complaining party. *Eastburn v. Ford Motor Co.*, 471 F.2d 21, 22-33 (5th Cir. 1972). Thus, even if the wrong standard of review was used, the error would be harmless if the conclusion of the appellate court would have been the same, regardless of the particular standard of review chosen. New trials will not be granted for errors of law which did not reach the merits; when upon the whole case, the judgment was plainly right. *M'Lanahan v. Universal Ins. Co.*, 26 U.S. 170, 183, 1 Pet. 170, 7 L.Ed. 98 (1828). Support for the proposition that any error in the present case in the selection of the standard of review was harmless can be shown by demonstrating that the outcome of the present case would be the same under any and all of the standards of review currently being used for Rule 11 issues.

"Abuse of discretion" is the most widely accepted standard of review and was the standard of review applied by the Tenth Circuit Court of Appeals to the Rule 11 issues presented by Petitioner. Exhibit H of the Petition, incorporated herein by reference, at page H-3. The appellate court expressly chose "abuse of discretion" as the appropriate standard of review, being quite aware that "abuse of discretion" was not the only standard of review currently being used with regard to Rule 11 issues. *Id.* In its opinion, the appellate court analyzed the facts and the law with regard to the Rule 11 issues presented by Petitioner as follows:

> Appellants alleged in their complaint that appellees had misrepresented the meaning of

> "prime rate" or "base rate" in negotiating a loan with appellants. However, appellants came forward with no evidence purported to show that appellees had made such misrepresentations. The Hills' depositions in a prior, nearly identical case indicated that neither of them was aware of any such statements by appellees. At the sanctions hearing, Ronald Hill finally testified that appellees made such misrepresentations, but the district court apparently discounted this eleventh-hour recollection. The Hills had never before presented testimony to this effect, either by deposition or affidavit, even in opposition to appellee's motion to dismiss. A reasonable inquiry would have uncovered the lack of support for the allegations against appellees in the Hills' original complaint.
>
> Appellants also appeal the district court's award of sanctions based on the amended complaint naming appellees as defendants after appellees had won summary judgment on the original complaint. Appellants argue that the failure to name appellees in their amended complaint would have waived the Hills' rights under their pending motion to reconsider and their right to appeal the district court's order granting summary judgment. Appellants present no case to support their proposition. We agree with the district court that including appellees in the amended complaint, and forcing them to defend themselves against the same accusations upon which they had already prevailed, was unreasonable and not warranted by existing law. Furthermore, the amended complaint perpetuated the deficiencies of the original complaint. We find no abuse of discretion by the trial court.

Exhibit H of the Petition at pages H-3 and H-4. *See also,* Exhibit E of the Petition, incorporated herein by reference, at pages E-2 through E-5. Thus, the Rule 11

sanctions against Petitioner were, in fact, upheld under an "abuse of discretion" standard of review.

These sanctions would also have been upheld under the "three-pronged" standard of review set out in *McMahon, Equal Employment Opportunity Comm'n*, and *Zaldivar*. The first prong requires that the factual determinations of the district court be reviewed under the clearly erroneous standard. 780 F.2d at 828. The Petitioner, however, has been unable to place in issue any particular factual determination by the district court. Thus, the first prong need not be addressed in the present case.

The second prong of this alternative standard of review requires that the legal conclusion of the district court (that the facts constituted a violation of Rule 11) be reviewed *de novo*. *Id*. The facts in the present case clearly demonstrate, on *de novo* review, that the Petitioner did not make a reasonable inquiry before filing the complaint or the amended complaint to determine if such pleadings were well grounded in fact and were warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law. Support for this proposition can be found in several instances cited in the Statement of Facts, Appendix B. First, no evidence was offered to demonstrate, *prior* to the filing of the original complaint, that there was a factual basis for claiming that Respondents had made misrepresentations. In fact, the Hills' depositions in a prior, nearly identical case evidenced their lack of awareness of any such statements by Respondents. Statement of Facts, Appendix B, at pages B-1 through B-2. The district court correctly discounted

the eleventh-hour recollection of Ronald Hill, at the sanctions hearing, that Respondents made such misrepresentations. As the appellate court noted "[T]he Hills had never before presented testimony to this effect, either by deposition or affidavit, even in opposition to appellee's motion to dismiss." Exhibit H of Petition at page H-4. The only basis for the fraud claim appears to have been the Hills' own misconceptions. Statement of Facts, Appendix B, at pages B-1 through B-2. Second, Ronald Hill was a director of UOB and had access to loan information during the time in which he claimed to be defrauded. Consequently, Ronald Hill was *precluded* as a *matter of law* from bringing a claim based upon common law fraud. Statement of Facts, Appendix B, at pages B-2 through B-3. Third, the only two non-party witnesses called by the Petitioner during the sanctions hearing both testified they first met Petitioner and related their testimony on the very morning of such sanctions hearing! Statement of Facts, Appendix B, at page B-5. One witness conceded her knowledge was based on hearsay and never testified Respondents made false statements. Statement of Facts, Appendix B, at page B-5. The other non-party witness had no knowledge of Respondents' involvement in any loans that allegedly carried a lower interest rate than the prime rate. Statement of Facts, Appendix B, at page B-5. Finally, the Petitioner filed an amended complaint naming the Respondents *after* the Respondents had already obtained a judgment on the merits in their favor! Statement of Facts, Appendix B, at pages B-3 through B-4. A reasonable inquiry would have uncovered the lack of support for the allegations against Respondents contained in both the original complaint and the amended

complaint. Based upon a *de novo* review, it is clear that Petitioner violated Rule 11, and the imposition of sanctions was justified.

The third prong requires that the appropriateness of the sanction be reviewed for an "abuse of discretion." 780 F.2d at 828. However, Petitioner has never placed the "appropriateness" of the sanction in issue by objecting either to the type or amount of the sanction. Consequently, review under the third prong is not required.

This analysis of the present case under the "three-pronged" standard of review reveals that the appellate court's conclusion would be unchanged; the Rule 11 sanctions awarded against Petitioner were justified and would be upheld.

The remaining standard of review as set out in *Donaldson* and *Westmoreland* differs depending on the question before the court. First, a decision as to whether a pleading or a motion is legally sufficient is reviewed *de novo*. 819 F.2d at 1556. In the present case, Petitioner filed a complaint on behalf of the Hills, alleging common law fraud; but as a *matter of law*, Ronald Hill could not bring such a claim, since he was a director of UOB and had access to loan information during the times in which he claimed he was defrauded. Statement of Facts, Appendix B, at pages B-2 through B-3. In addition, the Petitioner filed an amended complaint naming Respondents, *after* Respondents had already obtained a judgment on the merits in their favor! Statement of Facts, Appendix B, at pages B-3 through B-4. *De novo* review clearly demonstrates that Petitioner failed to make a reasonable inquiry to determine if the original complaint and the amended

complaint were warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law. This failure justified the imposition of Rule 11 sanctions on Petitioner.

Second, whether factual or bad faith reasons exist to impose Rule 11 sanctions and the "appropriateness" of the particular sanction are reviewed for an "abuse of discretion." 819 F.2d at 1556. As Petitioner has not placed the "appropriateness" of the sanctions in issue, only the factual or bad faith reasons for sanctions will be analyzed. In the present case, no evidence was offered to demonstrate, *prior* to the filing of the original complaint, that there was a factual basis for claiming that Respondents had made misrepresentations. The evidence does suggest that the only basis for the allegations of fraud was the Hills' own misconceptions! *See* Statement of Facts, Appendix B, at pages B-1 through B-2. There is no evidence in the record that Petitioner conducted any independent inquiry prior to filing the Complaint. Indeed, except for depositions given by the Hills in a prior, nearly identical case, no evidence was offered to the district court that Petitioner obtained *any* investigative or discovery material prior to filing the complaint. Further, the only evidence as to the reasonableness of filing the amended complaint was provided by Respondents' expert witness, Andrew M. Coats. Such evidence indicated that the filing of the amended complaint was unreasonable. This testimony additionally revealed that this case is an appropriate case for sanctions under Rule 11. Statement of Facts, Appendix B, at pages B-4 through B-5. Upon these facts alone and especially in conjunction with the more detailed Statement of Facts, Appendix B, the

trial court was justified in awarding Rule 11 sanctions and did not abuse its discretion.

This analysis of Petitioner's case using the standard of review set out in *Donaldson* and *Westmoreland* also reveals that the appellate court's conclusion would be unchanged; the Rule 11 sanctions awarded against Petitioner were justified and should be upheld.

"Abuse of discretion" was a correct standard of review, even if it was not the only one available. Assuming, however, that the wrong standard of review was used by the appellate court, such error was harmless, as the same conclusion would be reached in the present case regardless of the particular standard of review chosen. Under either scenario, the substantial rights of the Petitioner have not been impaired, and this case is not appropriate for review by the Supreme Court of the United States.

II

WHETHER THE SUBSTANTIVE LAW OF AMENDED COMPLAINTS CONTROLS PROCEDURAL LAW IS OF NO CONSEQUENCE, SINCE RESPONDENTS HAD ALREADY OBTAINED A JUDGMENT ON THE MERITS IN THEIR FAVOR.

The Petitioner's argument that the substantive law of amended complaints controls procedural law is irrelevant and of no consequence in the present case. The Petitioner contends that it was necessary to name the Respondents in the amended complaint to preserve his clients' claims against the Respondents in that cause. To the contrary, Respondents had already obtained a judgment on the merits in their favor at the time the amended complaint

was filed. Consequently, the Petitioner's clients had *no claims remaining* in this cause against the Respondents. The Petitioner preserved *nothing* on behalf of his clients by naming the Respondents in the amended complaint. The Petitioner did, however, through naming the Respondents in the amended complaint, demonstrate that he failed to make a reasonable inquiry into the facts to determine if the amended complaint was well grounded and to determine if it and the allegations contained therein were warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law as required by Rule 11.

CONCLUSION

For the reasons set forth above, Respondents respectfully request that this Court not issue a Writ of Certiorari on any of the questions presented.

Respectfully submitted,

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APPENDIX A

FEDERAL RULE OF CIVIL PROCEDURE, RULE 11

Rule 11. Signing of Pleadings, Motions and Other Papers; Sanctions.

Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in his individual name, whose address shall be stated. A party who is not represented by an attorney shall sign his pleading, motion or other paper and state his address. Except when otherwise specifically provided by rule or statute, pleadings need not be verified or accompanied by affidavit. The rule in equity that the averments of an answer under oath must be overcome by the testimony of two witnesses or of one witness sustained by corroborating circumstances is abolished. The signature of an attorney or party constitutes a certificate by him that he has read the pleading, motion or other paper; that to the best of his knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. If a pleading, motion or other paper is not signed, it shall be stricken unless it is signed promptly after the omission is called to the attention of the pleader or movant. If a pleading, motion or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other

party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper, including a reasonable attorney's fee.

APPENDIX B

STATEMENT OF FACTS

Prior to filing the present action, the Hills brought suit against United Oklahoma Bank ("UOB"), and subsequently the Federal Deposit Insurance Corporation ("FDIC"), as liquidating agent of the bank. Neither UOB nor the FDIC are parties to the present appeal. In that prior action, the Hills alleged identical causes of action as are pled in the present case but against UOB, and they relied on the same alleged "predicate acts" as the basis for their claims of common law fraud and RICO violations. (*See Hill Resources, Inc., et al. v. Federal Deposit Insurance Corporation*, Case No. CIV-87-267-R in the United States District Court for the Western District of Oklahoma) (hereinafter referred to as *"Hill v. FDIC"*). [Doc. 29 at 4].

In *Hill v. FDIC*, as well as another related proceeding, *Federal Deposit Insurance Corporation v. Hill Resources, Inc., et al.*, Case No. CIV-87-767-T in the United States District Court for the Western District of Oklahoma (hereinafter referred to as *"FDIC v. Hill"*), both of which were pending at the time the present suit was brought, discovery had been conducted based upon the identical fact situation as the present case. [Doc. 17 at 6].

In *FDIC v. Hill*, deposition testimony of Ronald Hill and Irving Hill, taken before the present action was filed, revealed that neither Kerr nor Johnstone represented to the Hills that the UOB prime rate or base rate was the best rate UOB charged its most credit-worthy commercial customers. [Doc. 21 at Exhibits "A" and "B"]. In fact, the testimony revealed that the basis of the Hills' claim of

fraud by Kerr and Johnstone was based on their own incorrect assumption that the terms "prime rate" and "base rate" were the best rates charged the bank's most credit-worthy commercial customers. [Doc. 21 at Exhibit "B"; Doc. 30 at 3].

Based upon this prior testimony of the Hills, on April 13, 1988, Kerr and Johnstone filed their Motion to Dismiss, attaching excerpts from these depositions, as well as the Affidavits of Kerr and Johnstone. [Doc. 21]. In their Affidavits, Kerr and Johnstone asserted that they never represented, nor directed any UOB employee to represent that the term "base rate" meant the rate available to UOB's most credit-worthy commercial borrowers. They further asserted that they did not use the United States mails, nor direct any UOB employee to use the United States mails to represent that the term "base rate" meant the rate available to UOB's most creditworthy commercial borrowers. [Doc. 21 at Exhibits "D" and "E"].

Kerr and Johnstone attached to their Motion to Dismiss the district court's order in *Hill v. FDIC*, whereby the court held that as a matter of law, Ronald Hill was precluded from asserting a claim based upon common law fraud since he was a director of UOB, and thus had access to information relating to the loans being made by UOB. [Doc. 21 at Exhibit "C"].

In their Brief in Opposition to the Motion to Dismiss, the Hills attached the Affidavit of Edwin J. Lippman, Jr. (the "Lippman Affidavit"), a former vice president and loan officer at UOB. [Doc. 28 at Exhibit "D"]. However, the Lippman Affidavit did not show that any fraudulent

representations were made to the Hills by either Kerr or Johnstone.

On September 13, 1988, the district court granted Kerr and Johnstone's Motion to Dismiss, treating it as a motion for summary judgment since matters outside of the pleadings were submitted by both parties. [Doc. 30 at 1]. The district court held that the Hills had failed to show any fraudulent acts by Kerr or Johnstone sufficient to state a claim based on common law fraud or RICO. Further, the district court held that as a matter of law, Ronald Hill was precluded from bringing an action based on common law fraud. [Doc. 30 at 3-4]. The district court also stated that since the Lippman Affidavit did not show that any fraudulent representations were made to the Hills by either Kerr or Johnstone, it could not be the basis for the Hills' fraud action. [Doc. 30 at 3].

On September 27, 1988, the Hills filed a Motion to Reconsider the district court's September 13, 1988 Order Granting Summary Judgment. [Doc. 33]. Only at this late stage in the proceedings, after judgment had been rendered in favor of Kerr and Johnstone, did Ronald Hill and Irving Hill prepare affidavits. Irving Hill represented that the loan officers at UOB made fraudulent representations to him, and Ronald Hill represented that specifically Kerr and Johnstone made these fraudulent representations to him. [Doc. 33 at Exhibits "A" and "B"].

On October 18, 1988, the district court denied the Hills' Motion to Reconsider. The district court specifically rejected evidence attached to the Motion to Reconsider, including the Affidavits of Ronald Hill and Irving Hill, since the Hills clearly had access to this information at

the time they filed their Brief in Opposition to the Motion to Dismiss. The district court also stated that "at least some investigation should have been done under Rule 11 of the *Federal Rules of Civil Procedure* before the Complaint was filed." [Doc. 40 at 2].

Based upon the clear lack of factual basis for the Hills' claims, on September 28, 1988, Kerr and Johnstone filed their Motion for Award of Attorney's Fees and Expenses pursuant to Fed. R. Civ. P. 11 [Doc. 34]. However, on October 6, 1988, the Hills filed their Amended Complaint, whereby they once again made allegations against Kerr and Johnstone, although arguably with greater particularity. [Doc. 36]. Since Kerr and Johnstone had already obtained judgment on the merits in their favor [Doc. 30], on October 25, 1988, they filed their motion to supplement their Motion for Award of Attorney's Fees and Expenses, adding, for the first time, claims against DeVore. [Doc. 44]. The Hills filed a response to the Motion for Award of Attorney's Fees and Expenses [Doc. 38], and the district court set these motions for a hearing on November 1, 1988 (the "November 1, 1988 Hearing").

At the November 1, 1988 Hearing, Kerr and Johnstone produced an expert witness, Andrew M. Coats ("Coats"), who testified that this case was not well grounded in fact when the Complaint was filed, based upon the previous deposition testimony of Ronald Hill and Irving Hill [Tr. 11/1/88 at 20-21, 25, 42-43], as well as the ruling against Ronald Hill in *Hill v. FDIC* [Tr. 11/1/88 at 45]. Coats further testified that the case was not well grounded in fact when the Amended Complaint was filed, since the district court had previously sustained a

motion for summary judgment in favor of Kerr and Johnstone. [Tr. 11/1/88 at 43].

The Hills produced Ann Pittenger ("Pittenger") and Robert Scott ("Scott"), former customers of UOB, as witnesses. However, upon cross-examination, it was revealed that Pittenger's knowledge of the alleged fraudulent representations was based on certain unidentified answers to interrogatories in unidentified litigation sometime in 1986. [Tr. 11/1/88 at 70-72]. No evidence was offered that either Kerr or Johnstone had any involvement in the loans which were the subject of the unidentified answers to interrogatories. Pittenger never testified that either Kerr or Johnstone ever made false statements. Finally, Pittenger revealed that she first met and related her testimony as to the alleged misrepresentations by Kerr and Johnstone to DeVore on November 1, 1988. [Tr. 11/1/88 at 70].

Scott testified merely that he was told UOB's prime rate "was the rate that (sic) bank gave its best commercial customers." [Tr. 11/1/88 at 74]. Interestingly this statement is materially different from the allegation that the rate was represented to be the "best rate for the bank's most credit-worthy customers". However, Scott never testified that Kerr or Johnstone had any involvement in any loans that allegedly carried a lower interest rate than prime. Further, Scott testified that he first met and related his testimony as to the alleged misrepresentations by Kerr and Johnstone to DeVore on November 1, 1988. [Tr. 11/1/88 at 82].

Ronald Hill also testified at the November 1, 1988 Hearing that he first learned that UOB had allegedly

made loans at less than prime rate or base rate in 1986 through his attorney, Herman Brandon. [Tr. 11/1/88 at 86]. When he learned in 1986 that UOB was allegedly making bank stock loans at less than prime rate or base rate, he testified that he spoke with the people who allegedly had these loans with UOB. However, he never physically examined the notes that were allegedly below prime rate or base rate. [Tr. 11/1/88 at 101].

Ronald Hill admitted that he did not research the applicable regulatory requirements as to interest rates that a bank must charge on bank stock loans, as well as loans secured by certificates of deposit, prior to bringing the present lawsuit. [Tr. 11/1/88 at 102, 109]. He also admitted that he first obtained documents which showed specific names of borrowers, the interest rates charged, and the amount loaned by UOB, *after* the Plaintiffs' lawsuit against the FDIC had settled. [Tr. 11/1/88 at 109, 113]. However, the Hills' lawsuit against the FDIC settled *after* the present lawsuit was filed. [Tr. 11/1/88 at 29]. Thus, although Ronald Hill testified that he reviewed the documentation received from the FDIC before filing the present action, and that he related this information to his attorney before filing the present action, this is physically impossible since Ronald Hill obtained the information from the FDIC *after* the present action was filed. [Tr. 11/1/88 at 29, 89, 113-114]. Accordingly, Ronald Hill had no physical evidence at the time he initially filed the present action [Tr. 11/1/88 at 108], and has offered only his own testimony, which has been impeached numerous

times [1], to purportedly show fraudulent conduct by Kerr and Johnstone.

Admittedly, the Hills acquired, in 1986, hearsay evidence that UOB purportedly made loans below its prime rate. [Tr. 11/1/88 at 108]. However, the Hills have offered no evidence that either Kerr or Johnstone had any involvement in the loans which were the subject of the hearsay evidence, and have conceded that Kerr and Johnstone left UOB in 1985 and possibly as early as 1984. [Tr. 11/1/88 at 95-96].

Irving Hill testified at the November 1, 1988 Hearing that he first learned that UOB was allegedly making loans to other customers at rates lower than prime rate or base rate in 1986 from Ronald Hill and from his attorney, Herman Brandon. [Tr. 11/1/88 at 122-123]. However, in his Affidavit attached to the Motion to Reconsider dated September 27, 1988, allegations by Irving Hill against Kerr and Johnstone as to alleged fraudulent representations are notably missing. [Doc. 33 at Exhibit "A"; Tr. 11/1/88 at 131, 133].

Irving Hill also revealed that he made no investigation into the applicable statutes and regulations with respect to interest rates that a bank must charge on certain types of loans. Further, he never requested that his attorney research the applicable statutes and regulations

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[1] While not an exhaustive list of instances which question Ronald Hill's credibility, *See* Tr. 11/1/88 at 94, 98 and 101-102. Further, Ronald Hill has testified the Hills had only one fixed rate loan [Tr. 11/1/88 at 109], when, in truth and in fact, many of their loans were either fixed rate or were a combination of fixed rate and variable rate notes. [Doc. 21 at Exhibit "A"].

with respect to interest rates that a bank must charge on certain types of loans. [Tr. 11/1/88 at 137].

Finally, although Irving Hill initially testified that Johnstone had made representations to him as to the meaning of the term prime rate or base rate, further questioning as well as an examination of previous testimony under oath revealed that no representations as to the meaning of the term base rate or prime rate were made by Kerr or Johnstone to him. [Tr. 11/1/88 at 116, 128, 134].

As a final point, it should be noted that there is no evidence in the record that DeVore conducted any independent inquiry prior to filing the Complaint. Indeed, except for depositions given by the Hills in *FDIC v. Hill*, no evidence was offered to the district court that DeVore obtained *any* investigative or discovery material prior to filing the Complaint. Further, the only evidence as to the reasonableness of filing the Amended Complaint was provided by Coats, Kerr's and Johnstone's expert witness. Such evidence indicated that the filing of the Amended Complaint was unreasonable. [Tr. 11/1/88 at 43]. This testimony additionally revealed that this case is an appropriate case for sanctions under Fed. R. Civ. P. 11. [Tr. 11/1/88 at 21].